(2)

No. 91-369

In the Supreme Court of the United States

OCTOBER TERM, 1991

LILTON CHESSON, JR., AND
RANDALL CHESSON, PETITIONERS

v.

UNITED STATES OF AMERICA

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*ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT*

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether the evidence was sufficient to establish a tax deficiency.

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OPINION BELOW

The opinion of the court of appeals (Pet. App. 1-20) is reported at 933 F.2d 298.

JURISDICTION

The judgment of the court of appeals was entered on June 3, 1991. The petition for a writ of certiorari was filed on August 30, 1991. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Following a jury trial in the Western District of Louisiana, petitioners were each convicted on three counts of willfully attempting to evade income tax, in violation of 26 U.S.C. 7201, and on one count of conspiracy to defraud the United States by impairing and impeding the lawful governmental functions of the Internal Revenue Service (IRS), in violation of 18 U.S.C. 371. Pet. App. 2.

1. The evidence at trial showed that petitioner Lilton Chesson was the chief executive officer of Chesson Oil Corporation and its sister company, Cameron Offshore Services. Pet. App. 2-3. Lilton and petitioner Randall Chesson were the sole shareholders of the companies. Randall was also the full-time pastor of Parkview Baptist Church and assisted Lilton in managing the companies. Pet. App. 3.

From 1981 through 1983, the companies paid a large amount of petitioners' personal expenses, including expenditures for travel, vehicle repairs, sporting goods, electronic equipment, legal fees, jewelry, and other personal items that were billed to petitioners' corporate credit cards. Pet. App. 4-5. Employees in the companies' accounting department knew the corporations were paying petitioners' personal expenses. The invoices for personal expenses were routinely processed and paid in the same manner as those for legitimate business expenses. Pet. App. 5. As a matter of routine, the accounting department altered the designation of the addressee on invoices sent to the petitioners' residences. Pet. App. 5-6.

From 1981 through 1983, the corporations also paid almost $700,000 for the renovation and reconstruction of the Parkview Baptist Church and school. Pet. App. 5-6. Lilton told a field supervisor for the

companies to charge the cost of the project to the repairs and maintenance account on the companies' books. Pet. App. 6. Some of the church-related invoices were altered to obliterate the name of the church or other "church-related references." *Ibid.*

During the three years at issue, the companies paid personal expenses of more than $285,000 and church-related expenses in excess of $300,000. Approximately 700 invoices relating to non-corporate expenses were processed through the companies. Pet. App. 7-8. During the years at issue, the companies processed as many as 10,000 invoices per year. Pet. App. 3.

In 1980, the IRS audited the 1978 corporate tax return of Chesson Oil Corporation. The IRS disallowed payments for personal expenses of petitioners and for church-related expenses. The payments for personal items were charged as additional compensation to petitioners and resulted in increased personal tax liabilities for them. The payments for church-related items were allowed as corporate charitable contributions. Pet. App. 7.

In spite of the results of the IRS audit in 1980, petitioners continued to have the corporations pay large amounts of their personal and church-related expenses. During 1981 through 1983, the companies retained two accounting firms to develop year-end financial statements and to render unqualified opinions as to their material accuracy. Pet. App. 7. The accounting firms sent auditors to the companies. Although the auditors dealt with the head of the accounting department and had access to all corporate financial records, apparently neither accounting firm discovered that the companies were paying personal and church expenses and characterizing those payments as business expenses. *Ibid.*

2. The court of appeals affirmed petitioners' convictions. Pet. App. 1-20. On appeal, petitioners contended, *inter alia*, that there was insufficient evidence of a tax deficiency. They contended that their accountants should have reclassified the personal and church-related expenses as loans to petitioners. Pet. App. 16. The court of appeals rejected that contention. The court held that the expenditures could not be reclassified as shareholder loans without evidence that petitioners had intended to take loans from the corporations at the time the payments were made. Pet. App. 16-18.[1]

ARGUMENT

To establish a violation of 26 U.S.C. 7201, the government must prove (1) the existence of a tax deficiency, (2) an affirmative act of evasion or attempted evasion of the tax due, and (3) willfulness. *Sansone* v. *United States*, 380 U.S. 343, 351 (1965); *United States* v. *Helmsley*, No. 90-1012 (2d Cir. July 30, 1991), slip op. 6590-6591; *United States* v. *Williams*, 875 F.2d 846, 849 (11th Cir. 1989). Petitioners argue (Pet. 8-15) that the evidence was insufficient to support the jury's findings that there was a tax deficiency. They assert (Pet. 8-9) that the only proof of a tax due and owing was an IRS revenue agent's "after-the-fact classification of certain corporate business expenditures for personal items as taxable constructive dividends," while the evidence at

[1] The court of appeals also rejected petitioners' arguments that the evidence was insufficient to show that petitioners acted willfully and conspired to obstruct the tax collecting function of the IRS, and that the district court erred by admitting an invoice into evidence. Pet. App. 10-16, 18-20. Petitioners do not pursue those arguments here.

trial showed that petitioners' accountants could have reclassified the expenses as loans to shareholders and thereby eliminated any additional tax liability to petitioners or the companies. Petitioners' argument is meritless.[2]

In order to prove the existence of a tax deficiency, the government must prove (1) that the defendant had unreported income, and (2) that the income was taxable. *United States* v. *Hiett*, 581 F.2d 1199, 1200 (5th Cir. 1978). The government establishes a *prima facie* case by proving the defendant's receipt of funds having the appearance of income. See *United States* v. *Fogg*, 652 F.2d 551, 553-555 (5th Cir. 1981), cert. denied, 456 U.S. 905 (1982); *United States* v. *Miller*, 545 F.2d 1204, 1215 n.13 (9th Cir. 1976), cert. denied, 430 U.S. 930 (1977); *United States* v. *Lacob*, 416 F.2d 756, 760 (7th Cir. 1969), cert. denied, 396 U.S. 1059 (1970); *United States* v. *Garcia*, 412 F.2d 999, 1001 (10th Cir. 1969). It is well settled that a shareholder's willful diversion of corporate funds to pay his personal expenses renders the shareholder criminally liable for understating his personal income. See *United States* v. *Thetford*, 676 F.2d 170, 175 (5th

[2] Petitioners also assert (Pet. 9) that allowing the IRS to reclassify the expense payments as income impermissibly relieved the government of its burden of proving a tax deficiency. As discussed further below, however, the fact that the payments were made for petitioners' benefit, and were not treated as loans on the corporations' books, established a *prima facie* case of a tax deficiency. Although petitioners risked conviction if they failed to rebut the government's *prima facie* case, that is not the same as shifting the burden of proof. See *Holland* v. *United States*, 348 U.S. 121, 138-139 (1954) (rule that government is not required "to negate every possible source of nontaxable income" in a net worth case does not shift burden of proof; "[o]nce the Government has established its case, the defendant remains quiet at his peril.").

Cir. 1982), cert. denied, 459 U.S. 1148 (1983); *United States* v. *Miller, supra; Bernstein* v. *United States*, 234 F.2d 475 (5th Cir.), cert. denied, 352 U.S. 915 (1956); *Davis* v. *United States*, 226 F.2d 331 (6th Cir. 1955), cert. denied, 350 U.S. 965 (1956).

The court of appeals properly found (Pet. App. 16-18) that the evidence at trial, viewed in the light most favorable to the government, was sufficient to support the jury's finding that the corporate funds that were used to pay petitioners' personal expenses constituted taxable income to them rather than loans. Petitioners concede that their companies paid approximately $285,000 of their personal living expenses during the years at issue. Pet. 5. They also concede (Pet. 4-6) that while the corporate ledgers had accounts for shareholder loans (Pet. App. 17), none of the expenditures for petitioners' personal living expenses was recorded as a loan.

Evidence that the companies' accountants could have reclassified the payments at issue as loans (see Pet. App. 16) was insufficient to rebut the government's case. As this Court has held, "[t]ax consequences follow [from] what has taken place, not what might have taken place." *Central Tablet Mfg. Co.* v. *United States*, 417 U.S. 673, 690 (1974). See also *Commissioner* v. *National Alfalfa Dehydrating & Milling Co.*, 417 U.S. 134, 148-149 (1974). In accord with this principle, the courts of appeals generally have refused to allow a criminal defendant to take advantage of some technical approach to the determination of his reporting obligations or tax liability that does not comport with the course actually followed by the defendant. See *United States* v. *Helmsley*, No. 90-1012 (2d Cir. July 30, 1991), slip op. 6595-6600; *United States* v. *Santarelli*, 778 F.2d

609, 617 (11th Cir. 1985); *United States* v. *Cruz*, 698 F.2d 1148 (11th Cir.), cert. denied, 464 U.S. 960 (1983).

Allowing a defendant to avoid prosecution simply by changing his accounting for payments on the eve of trial "would make a mockery of the federal income tax system." *United States* v. *Santarelli*, 778 F.2d at 617. An accused taxpayer in petitioners' position could have his corporation pay all of his bills, deduct the payments as business expenses on the corporate tax returns, and then, if caught, simply reclassify the payments as loans. See *United States* v. *Cruz*, 698 F.2d at 1150-1152; *United States* v. *Helmsley*, slip op. 6597.

The fact that an accountant classifies the payment of a corporate shareholder's personal expenses as a loan is not controlling. See *United States* v. *Pomponio*, 563 F.2d 659, 663 (4th Cir. 1977), cert. denied, 435 U.S. 942 (1978). The question is whether a payment is in fact a loan, not how an accountant has classified the payment. For the payment to constitute a loan, the shareholder must intend to repay it. *United States* v. *Pomponio*, 563 F.2d at 662.

Here, the jury had ample reason to find that the payments at issue were not loans. Petitioners offered no evidence that they ever intended to treat the expenditures as loans. Petitioners never repaid the corporation for any of the expenditures, and there was no indication that they ever intended to do so. On the contrary, petitioners' conduct strongly indicated that they had no intent to repay. After the IRS audited Chesson Oil in 1980, petitioners had increased personal income tax liabilities resulting from the disallowance of personal expenses that were originally characterized as business expenses. Pet. App. 7.

Even though the problem of the companies' payment of their personal expenses was brought to their attention by the IRS, petitioners failed to change their practices or alert their accountants to the issue. The jury thus had an amply sufficient basis for concluding that petitioners did not intend to repay the corporations, but instead sought to avoid personal income taxes by characterizing personal income as deductible corporate business expenses. See *United States* v. *Scott*, 660 F.2d 1145, 1162 (7th Cir. 1981) (jury could have decided that "gifts" were compensation for official acts), cert. denied, 455 U.S. 907 (1982); *United States* v. *Bianco*, 534 F.2d 501, 505 (2d Cir.) (jury could have disbelieved defendant's cash hoard defense), cert. denied, 429 U.S. 822 (1976).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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